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Office of Administrative Law Judges
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Issue date: 29Oct2001

CASE NO.: 1998-JTP-6

In the Matter of

COMMONWEALTH OF MASSACHUSETTS

Complainant

v.

U.S. DEPARTMENT OF LABOR

Respondent

DECISION AND ORDER

I. Statement of the Case

This case, which arises under the Job Training Partnership Act (the JTPA), 29 U.S.C. §1501 *et seq.*, and the implementing regulations found at 20 C.F.R. Parts 626-638, is before the Office of Administrative Law Judges of the U.S. Department of Labor on a request for hearing filed by the Complainant Commonwealth of Massachusetts (the Commonwealth) which seeks review of a final determination by the Grant Officer for the Employment and Training Administration (ETA) of the Respondent U.S. Department of Labor (the Department) to disallow certain costs under the JTPA. Section 166 of the JTPA, 29 U.S.C. §1576, provides in relevant part that a JTPA funds recipient, upon whom a corrective action or a sanction has been imposed by the Secretary of Labor, may request a hearing before an administrative law judge. *See also* 20 C.F.R. §§627.800, 627.801(a).

The final determination under appeal was issued to the Commonwealth on May 13, 1998 by the Grant Officer, disallowing \$9,107,986 in costs under the JTPA for 1994, 1995 and 1996. Respondent's Exhibit GX 1-4a-b.¹ As will be discussed in greater detail below, the Grant Officer's final determination followed from an administrative decision by the Commonwealth, as the recipient of the JTPA funds in question, to disallow costs assessed against these funds by a subrecipient, the City of Lynn, Massachusetts. On May 29, 1998, the Commonwealth appealed the final determination to the

¹ Documentary evidence in the record is identified as "CX" for exhibits offered by the Complainant, "GX" for exhibits offered by the Respondent and "ALJX" for exhibits introduced by the Administrative Law Judge. References to the hearing transcript will be designated as "TR".

Office of Administrative Law Judges. GX 1-2. Pursuant to a pre-hearing order issued by the Chief Administrative Law Judge on June 18, 1998, ALJX 2, the Commonwealth filed a pre-hearing memorandum on September 28, 1998, at which time it identified the following issues to be decided in connection with its appeal of the Grant Officer's final determination: (1) whether the Commonwealth is entitled to a waiver of the disallowed costs under section 164(e)(2) of the JTPA; (2) whether this proceeding should be stayed pending the outcome of the City of Lynn's appeal in state court; (3) whether the amount of \$9,107,986 disallowed by the Grant Officer is correct; and (4) whether the Grant Officer has met her burden of production. ALJX 7.²

The matter was originally assigned to District Chief Judge David W. Di Nardi who scheduled a hearing for February 8, 1999. ALJX 10. On December 31, 1998, the Commonwealth moved to stay the proceedings before the Office of Administrative Law Judges pending the outcome of an appeal filed in state court by the City of Lynn seeking review of the Commonwealth's decision to disallow \$9,160,208 in costs under the JTPA program for 1994, 1995 and 1996. ALJX 11. By order issued on January 12, 1999, Judge Di Nardi denied the Commonwealth's motion for a stay based on his finding that the outcome of the City of Lynn's appeal in state court is not material to the issues in instant case. ALJX 14. Thereafter, the case was reassigned to me. ALJX 17.

Prior to the hearing on the merits, the Department filed a motion for summary judgement, in which it asserted that there are no material facts in dispute and urging that the Grant Officer's final determination be affirmed. ALJX 15. The Commonwealth filed an opposition to the Department's motion, and it requested to be heard at an oral argument. ALJX 21. I granted the Commonwealth's request for oral argument on the motion, ALJX 23, and a limited hearing was conducted before me in Boston, Massachusetts on February 8, 1999 at which time both parties presented their arguments on the Department's motion for summary judgement. In addition, the parties were allowed to file briefs.

On April 14, 1999, I issued an order denying the Department's motion for summary judgement based on my finding that there were material issues of fact relating to the proper amount of disallowed costs and whether a waiver of liability was appropriate. I further found upon review of the proceedings before the Grant Officer that the Commonwealth had not been provided with an opportunity to submit evidence to mitigate the amount of disallowed costs and that there had been confusion regarding the Commonwealth's right to request a waiver of its liability for any disallowed costs. Accordingly, I remanded the case to the Grant Officer with instructions to: (1) provide the Commonwealth with an opportunity pursuant to 20 C.F.R. §627.606(c) to submit evidence in support of its position that its liability should be reduced to the extent that it can demonstrate that any of the disallowed costs were expended in conformity with the requirements of the JTPA and regulations, and an opportunity to

² The Commonwealth filed a supplemental pre-hearing memorandum on January 15, 1999, but raised additional issues. ALJX 16.

request a waiver of its liability pursuant to 29 U.S.C. §1574(e)(2) and 20 C.F.R. §627.704; and (2) issue a revised written final determination pursuant to 20 C.F.R. §627.606(d) after consideration of any evidence and argument presented by the Commonwealth if the matter was not fully resolved on remand. *Commonwealth of Massachusetts v. U.S. Department of Labor*, USDOL/OALJ Reporter (HTML), OALJ No. 1998-JTP-6 (ALJ April 14, 1999); ALJX 1A.

Pursuant to the April 14, 1999 order, the Grant Officer sent a letter dated April 29, 1999 to the Commonwealth, inviting it to submit any documentation not previously submitted to either the Grant Officer or the Administrative Law Judge, regarding the amount of disallowed costs and waiver of liability. GX 5. The Commonwealth responded on June 28, 1999 by requesting the Department to review documentation relating to the disallowed costs and by requesting a waiver of liability for the disallowed costs. GX 3 at 1-6. The parties were unable to arrive at an informal resolution on remand, and the Grant Officer issued a Revised Final Determination again disallowing \$9,107,986 in costs under the JTPA for Fiscal Years 1994, 1995 and 1996. The Grant Officer also determined that the Commonwealth's request for a waiver of its liability for repayment of the disallowed costs failed to demonstrate compliance with the applicable statutory and regulatory criteria. GX 2 at 5-18. Thereafter, the Grant Officer filed an Updated Administrative File and a Second Updated Administrative File. GX 2, 3. Upon docketing of the updated Administrative File, the matter was scheduled for hearing in Boston, Massachusetts on September 19-21, 2000, at which time both parties appeared and were afforded an opportunity to present additional evidence and argument. At the close of the hearing, the record was held open at the parties' request for submission of post-hearing briefs which were timely filed by both parties. The record is now closed, and the matter is ready for decision.

II. Findings of Fact and Conclusions of Law

A. Background

1. The JTPA

The JTPA was passed by the Congress to establish programs designed to prepare youth and adults facing serious barriers to employment for participation in the labor force by providing job training and other services that will result in increased employment and earnings, increased educational and occupational skills, and decreased welfare dependency, thereby improving the quality of the work force and enhancing national productivity and competitiveness. 29 U.S.C. §1501. As pertinent to this case, the JTPA provides for grants from the federal government to the states to fund educational assistance and training programs. 29 U.S.C. §1506. The JTPA and implementing regulations provide detailed guidelines governing the expenditure of JTPA funds by state recipients and their subrecipients and for the monitoring and investigation of grants to insure compliance with the JTPA and regulations. 29 U.S.C. §§1571-1583; 20 C.F.R. §§627.400-629.495. These oversight and compliance procedures include requirements for audits at both the state recipient and federal levels; 29 U.S.C. §§1574, 1575; 20 C.F.R. §627.480; and they mandate administrative complaint and grievance hearing procedures at

local, state and federal levels. 20 C.F.R. §§627.501-627.504, 627.601-627.607. Reports of audits conducted by a recipient of JTPA funds must be provided to the Department's Office of Inspector General (OIG); 20 C.F.R. §627.480(c); and reports of federal level audits, which are conducted by the OIG or the Comptroller General, 29 U.S.C. §1575(b), are provided to the ETA Grant Officer. 20 C.F.R. 627.602(a)(1). Upon receipt of an audit report from the OIG, the Grant Officer is required to notify the recipient of the investigative findings and allow the recipient a period of time not to exceed 60 days in which to comment and take appropriate corrective action. *Id.* In cases where the Grant Officer is dissatisfied with a state's disposition of an audit, the Grant Officer must make an initial determination, 20 C.F.R. §627.606(b), and then provide the recipient with an opportunity, called the informal resolution period, to present documentation or arguments to resolve the matters in controversy before revoking a grant or imposing corrective action or sanctions. 20 C.F.R. §627.606(c). If the matter is not resolved informally, the Grant Office issues a final determination, 20 C.F.R. §627.606(d), and the recipient may then request a hearing before an administrative law judge. 20 C.F.R. §627.801(a).

2. The JTPA Grants in Issue

Pursuant to the provisions of the JTPA, the Commonwealth and the Department entered into grant agreements under the JTPA for Fiscal Years 1994, 1995 and 1996. The agreements designated the Commonwealth's Executive Office of Economic Affairs (EOEA)³ as the grant recipient of the JTPA funds. GX 8-10. EOEA then designated two of its agencies to disseminate and monitor the expenditure of the JTPA funds. The Massachusetts Department of Employment and Training (DET) was delegated responsibility for JTPA Title II funds, and the Massachusetts Industrial Services Program (ISP)⁴ was delegated responsibility for JTPA Title II funds. These agencies, in turn, disseminated the grant funds to 16 subrecipient Service Delivery Areas (SDAs) including the subrecipient SDA involved in this proceeding which is variously referred to as the Southern Essex SDA, Northshore SDA or Lynn SDA. ALJX 21 (affidavits of Alice Sweeney and Elisabeth Durkin).

3. The Grant Officer's Disallowance of JTPA Costs

On May 18, 1995, the Commonwealth filed an incident report with the Department's OIG, stating that the grant monitoring activities of the DET and CBWL/ISP had identified financial mismanagement of JTPA funds by the subrecipient City of Lynn and Northshore Employment Training (NET), the administrative entity for the Lynn SDA. GX 26. On October 10, 1995, the

³ As a result of a 1997 reorganization, the EOEA's responsibilities were assigned to two agencies, the Department of Economic Development (DED) and the Department of Labor and Workforce Development (DLWD). TR 38-39.

⁴ The ISP was subsequently renamed as the Corporation for Business, Work and Learning. M.G.L. c. 43, §165 (1997). The agency is referred to herein as "CBWL/ISP".

Commonwealth designated the Lynn SDA and NET as a “high risk” subrecipient pursuant to 29 C.F.R. §627.423 which authorizes the imposition of funding restrictions on the subrecipient. GX 24. On November 16, 1995, the Commonwealth issued notification of initial findings to Patrick J. McManus, the Mayor of Lynn and lead elected official for the Lynn SDA , questioning \$8,511,695.96 in costs under JTPA programs for 1994 through 1996. GX 23. Thereafter, on March 26, 1996, the Commonwealth served Mayor McManus notice of its final findings and determination to disallow \$1,565,352 in JTPA costs for 1994-1996 and questioning an additional \$7,153,774 in JTPA costs pending completion of an independent audit. GX 21. By letter dated April 10, 1996, the DET notified NET that its fiscal system had been decertified for the following reasons:

The review demonstrated that the fiscal systems maintained by NET are not operational or coherent and cannot be certified. NET failed to adequately implement the mutually agreed upon Corrective Action plan during the period beginning March 20, 1995 through the most recent monitoring on March 8, 1996. The fiscal systems fail to safeguard the integrity of JTPA funds and programs, making it clear that NET cannot be viewed as a viable entity to administer the JTPA Program for Fiscal Year 1997.

GX 20. This final determination was subsequently revised on August 5, 1997 and August 7, 1997 with a final disallowance of \$9,160,208 in JTPA costs for 1994-1996. GX 13, 18.

On April 11, 1996, the City of Lynn appealed DET’s March 26, 1996 final findings and determination, and the matter proceeded to a hearing before a DET Hearing Officer. While the City of Lynn’s appeal was pending, the Auditor of the Commonwealth issued a State Auditor’s Report on September 11, 1996 concerning NET’s income and expenditures for Fiscal Years 1995 and 1996, and on a limited basis for Fiscal Year 1994. GX 1 at 161-185. In that report, the Auditor found that NET had failed to maintain an adequate accounting system and conduct annual audits, and he recommended that an independent private accountant be retained to evaluate the situation and determine what must be accomplished to develop credible financial statements for NET for fiscal years 1995 and 1996. *Id.* at 175-176.

On February 20, 1997, the DET Hearing Officer issued a recommended decision upholding the disallowance of \$6,340,397 in JTPA costs after finding that the sole issue raised by the City of Lynn’s appeal was its liability to repay the disallowed costs. GX 16. On February 28, 1997, the DET Deputy Director adopted the Hearing Officer’s findings and recommended decision as his final decision. GX 16 at 1. The City of Lynn then filed a civil action in state Superior Court seeking review of the DET Deputy Director’s decision pursuant to M.G.L. c. 30A, §14.⁵

⁵ M.G.L. c. 30A, §14 provides that, except where expressly precluded by law, any person aggrieved by a final decision of a state agency in an adjudicatory proceeding may obtain judicial review of that decision where no statutory form of appeal or judicial review is provided by filing a civil action in

On March 13, 1997, the DET sent a letter to the City of Lynn notifying it that the Commonwealth was establishing a debt owed by the City of Lynn to the Commonwealth in the amount of \$6,340,397 and demanding repayment of that amount. GX 15. After an attorney representing the City of Lynn responded to this notice,⁶ the DET sent a letter dated April 17, 1997 to the City's attorney, requesting submission of a repayment plan and advising that "[a] request for waiver of liability in this matter is not appropriate as the JTPA Regulations . . . provide that a waiver of liability can be granted only when the misexpenditure of JTPA funds was not a violation of section 164(e)(1) of the Act,"⁷ including failure to maintain accepted standards of administration." GX 14.

It appears that the Commonwealth submitted a status report to the ETA Regional Administrator on July 11, 1997.⁸ By letter dated July 18, 1997, the ETA Regional Administrator, Robert J. Semler responded to the Commonwealth's status report. Mr. Semler complemented the Commonwealth's "continued diligence in the resolution of the City of Lynn/ Northshore Employment and Training disallowance issue" but expressed concern that "the City of Lynn has not yet established a repayment schedule with the Commonwealth for the previously established debt of \$6,340,397 and appears to be using all conceivable avenues to avoid its clear responsibility for repayment." CX 1. Although Regional Administrator Semler commended the Commonwealth for its "full and good faith effort" in resolving the matter, he cautioned that the Commonwealth, as the direct recipient of JTPA funds, was ultimately liable for any disallowances incurred by its subrecipients, and he stated that the Commonwealth was not eligible to request a waiver of its liability:

In the event that the Commonwealth is unable to collect these disallowed funds from the City of Lynn as the responsible sub-recipient, the U. S. Department of Labor will issue a Findings and Determination to the Commonwealth and will establish a debt for the entire amount of these funds against the Commonwealth. In accordance with Section 164(e)(1) of the Act, these funds may not be offset but must be repaid from funds other than funds received under JTPA.

superior court. In its opposition to the Grant Officer's motion for summary judgement, the Commonwealth stated that the Superior Court has remanded the matter to the Hearing Officer for clarification of his decision. ALJX 21. The record does not reflect the final disposition the appellate proceedings before the state superior court.

⁶ The correspondence from the City's attorney is not in record.

⁷ Section 164(e)(1) provides that a recipient shall be liable to repay funds granted under the Act upon a determination that the misexpenditure of funds was due to "willful disregard of the requirements of this Act, gross negligence, or failure to observe accepted standards of ministrations." 29 U.S.C. §1574(e)(1).

⁸ The status report is not in the record.

Further, as we have stated previously in our response to Senator Kennedy's inquiry on this matter (see enclosure), since these disallowed costs result from violations of Section 164(e)(1) of the JTPA legislation, the Commonwealth of Massachusetts is not eligible to request a State Waiver of Liability.

*Id.*⁹ As mentioned previously, DET issued a revised Final Findings and Determination on August 5, 1997, disallowing a total of \$9,160,208 in JTPA costs and establishing a revised debt in that amount against the City Of Lynn. GX 12.

On August 12, 1997, the OIG transmitted a final audit report to the ETA.¹⁰ GX 7. Following her receipt of the audit report, the Grant Officer issued an Initial Determination to the Commonwealth on January 20, 1998, tentatively disallowing \$9,107,986 in costs under the JTPA program for fiscal years 1994 through 1996. GX 5a-b. In arriving at this figure, the Grant Officer noted that the auditors had identified a total of \$7,189,920 in JTPA Title II costs which had been disallowed by the Commonwealth against the Lynn SDA for 1994-1996 but that \$52,222 in disallowed costs involved the Americorps program which is not under the purview of the Department of Labor. Accordingly, the Grant Officer found that the total in JTPA Title II disallowed costs was \$7,137,698 which, when added to an additional \$1,970,288 in JTPA Title III costs that had also been disallowed by the Commonwealth, brought the total in disallowed JTPA costs to \$9,107,986. *Id.* at 6.

The Commonwealth responded to the Initial Determination in a letter dated March 25, 1998 from the DLWD Director to the Grant Officer. GX 6. The DLWD Director advised that the City of Lynn had filed an action in Essex Superior Court seeking a declaratory judgement overturning the Commonwealth's administrative determination which established a debt against the City based on the alleged misexpenditure of JTPA funds. The Director also stated,

We suspect that a substantial amount of appropriate JTPA services were provided by Lynn during the relevant period. However, to date, the City has not identified any documents that we believe would satisfy USDOL's audit requirements in order to mitigate the amount of disallowed costs. We are hopeful that the Commonwealth will have access to information through the litigation pending in Superior Court which may, at some future date, permit us to petition USDOL to reduce

⁹ Subsequent to the hearing on the motion for summary judgement, the Department offered a copy of a May 16, 1997 letter from Regional Administrator Semler to Senator Edward M. Kennedy. Grant Officer's Reply to Complainant's Opposition to Motion for Summary Judgement, Exhibit 1.

¹⁰ It appears that the audit for the fiscal year ending on June 30, 1996 was conducted by Deloitte and Touche, LLP, CPAs, pursuant to OMB Circular A-128 and the Single Audit Act of 1984. GX 5b at 1. The audit report found that a total of \$7,189,920 in JTPA costs had been disallowed or questioned by the Commonwealth through its monitoring of the Lynn SDA. GX 7 at 48.

the disallowed costs. We therefore request that the record be kept open in this matter at USDOL to permit the Commonwealth the opportunity, at a later date, to make such a showing if the facts so justify.

Id. at 2. It does not appear that the Grant Officer ever responded to the Commonwealth's request to hold the record open for submission of additional documentation.

On May 13, 1998, the Grant Officer issued a Final Determination and demand for repayment of \$9,107,986 in disallowed JTPA costs to the Commonwealth. GX 4a-b. In her Final Determination, the Grant Officer acknowledged the Commonwealth's position as set forth in the March 25, 1998 response to the Initial Determination but concluded,

“The audit and the corrective action record establish that the State recipient took appropriate and diligent action, as set out [in] Section[s] 164(e)(2) and 164(b)(1) of the JTPA, in bringing to light and terminating subgrantee misexpenditures that constituted willful disregard of the requirements established at Section 164(e)(1) of the JTPA. The State has also complied with the applicable audit coverage, resolution and debt collection requirements set out at 20 C.F.R. 627.480, and 481. In spite of its efforts, the State has not been able to obtain repayment from the subrecipient or secure its cooperation in a resolution process that could reduce the debt to the State.” In light of the foregoing, this Final Determination is being issued unchanged from the initial determination.

Id., Final Determination at 2 (quotations in original).¹¹ Pursuant to section 164(d) of the JTPA, 29 U.S.C. § 1574(d), the Grant Officer directed the Commonwealth to repay the Department from non-federal funds. GX 4a. The Commonwealth's appeal and request for hearing were then filed on May 29, 1998. GX 2.

B. Evidence Relating to Disallowed Costs

Pursuant to my April 14, 1999 remand order, the Commonwealth was provided with an opportunity to submit additional documentation in support of its request to reduce the amount of costs disallowed for the Title II and Title III JTPA programs for Fiscal Years 1995 and 1996 and its request for a waiver of liability. GX 2 at 8-18. The Commonwealth's documentation relating to the disallowed costs and request for a waiver of its liability were reviewed by Dennis Lonergan, the Administrative Officer for the ETA's Boston Regional Office, and Mary T. Ward, Technical Assistance and Training Coordinator. TR 20-22, 184, 255-57, 267-68, 276-79 and 291. Based upon their reviews of the documents, Mr. Lonergan and Ms. Ward made recommendations to the Grant Officer, Jaime Salgado,

¹¹ The source of the quoted portion of the Grant Officer's concluding paragraph is unclear.

who incorporated their findings in his Revised Final Determination. TR 25, 80-82, 85. Mr. Salgado testified that, although Mr. Lonergan and Ms. Ward reviewed the documentation submitted by the Commonwealth, he retained the ultimate authority to accept or reject these recommendations and that the Revised Final Determination reflects his findings and decisions. TR 254-57. The Grant Officer's Revised Final Determination indicates that the Commonwealth submitted reconstructed financial records in order to support \$7,278,340 of the \$9,107,986 total of disallowed costs. GX 2 at 9; GX 3 at 5. The Grant Officer issued a Revised Final Determination again disallowing \$9,107,986 in costs under the JTPA for 1994, 1995 and 1996, primarily because the documentation submitted by the Commonwealth had not been subjected to an audit and because the Commonwealth itself had not accepted the costs reflected in the reconstruction when it disallowed such costs in the decisions issued to the City of Lynn SDA. GX 2 at 9.

1. The Commonwealth's Reconstructed Trial Balance for FY 1995

In its submission to the Grant Office on remand, the Commonwealth stated that it had been unable to obtain a Financial Status Report (FSR) for FY 1995 that was traceable to source documentation maintained by the Lynn SDA and that the Lynn SDA had retained a consultant to reconstruct the SDA's records. GX 3 at 2. In response to the Commonwealth's demand for a properly supported FSR, the Lynn SDA retained the services of a Certified Public Accountant (CPA) to oversee a reconstruction sufficient to produce an auditable set of financial records and a FSR for FY 95. *Id.* The documents were reviewed by fiscal representatives of the Executive Office of Economic Affairs and the Commonwealth's JTPA Title II and III oversight agencies, who decided that a full audit of the FSR was not necessary because they determined that the CPA's report was adequate. GX 3 at 3. The reconstructed documentation, which was submitted to the Grant Officer, includes an explanation of the record reconstruction procedures utilized by the CPA, including an explanation of the cost allocation procedures, a summary sheet of sources of income and expenses, balance sheets and profit/loss statements for JTPA and non-JTPA grants. GX 3 at 7-28. The Commonwealth also submitted monthly balance sheets that were used to compile the summary information. TR 32; GX 3 at 12-16. In its submission to the Grant Officer, the Commonwealth asserted that \$4,861,178 in JTPA Title II costs for FY 1995 should be allowed, but it acknowledged that the reconstruction revealed \$1,049,280 in potential disallowed costs. GX 3 at 3, 11.

The Grant Officer rejected the Reconstructed Trial Balance and supporting documentation submitted by the Commonwealth, primarily because the reconstruction was not verified by an audit and because the Commonwealth did not accept the costs reflected in the reconstruction in its disallowance decisions issued to the City of Lynn. GX 2 at 9. Mr. Lonergan, who reviewed the reconstructed trial balance documentation for the Grant Officer, noted that the Commonwealth itself believed that the reconstruction needed to be verified by an audit, though an audit was never performed. TR 36. He further noted that the state auditors did not accept the documentation, instead recommending that an independent accountant be retained to develop credible financial statements, and that the Commonwealth had rejected the reconstructed trial balance documentation in the disallowance

decisions issued to the City of Lynn. TR 37-38; GX 1 at 174-176. On these considerations, Mr. Lonergan concluded that the reconstructed trial balance documentation was not supported by source documentation and that the allowableness of the costs was not verified by an audit. TR 39-40. The Grant Officer adopted Mr. Lonergan's recommendations and stated repeatedly in his Revised Final Determination that the documentation concerning the costs which the Commonwealth seeks to have allowed should be subjected to an audit pursuant to OMB Circular A-133 or a special procedures audit. GX 2 at 9-12.

2. Weekly Invoice Documentation for FY 1996 JTPA Title II Costs

Following the discovery of deficiencies in the Lynn SDA's financial systems in 1995, the Commonwealth imposed restrictions and modified its system for release of JTPA Title II funds to the Lynn SDA for FY 1996. GX 3 at 3. David Manning, the Commonwealth's JTPA Program Director, testified that the restrictions required the Lynn SDA to submit certain documentation to the Commonwealth prior to the release of JTPA funds. TR 406, 451. The modifications consisted of controls which were instituted to estimate cash needs based upon average weekly payroll and vendor warrants. *Id.* Subsequently, the Commonwealth further modified the cash release system to require specific backup documentation for all cash advances. GX 3 at 3. This backup documentation included payroll lists and a payment voucher recap sheet which shows a list of vendors with the amount owed each vendor from the funds advanced. *Id.* As examples of the documentation required under the restrictions, Mr. Manning referred to the Commonwealth's June 28, 1999 correspondence to the ETA Regional Administrator. GX 3. He testified that the documents appended to the Commonwealth's correspondence were submitted by NET to support their request for JTPA funds, and he explained that the documents at found at pages 67-69 cover staff costs as JTPA Title II training programs are mostly conducted in-house. TR 408-409. Mr. Manning further testified that the records located at pages 62-71 of GX 3 are a fair representation of the documents furnished to the ETA Regional Administrator. TR 412. Mr. Manning also testified that in addition to requiring detailed documentation, DET staff made on-site visits to NET before releasing requested JTPA funds to verify that NET spent the funds for the purpose requested. TR 451. He stated NET's payroll records, including time sheets, were reviewed on these visits. In addition, he testified that DET officials verified vendor checks against bank statements and, in some cases, contacted vendors to insure that they had received the checks from NET. TR 453. Mr. Manning thus testified that the funding restrictions and verification procedures implemented in FY 1996 enabled DET to verify that the Lynn SDA spent JTPA funds for the purposes for which they were provided. TR 453-54, 465.

In its June 28, 1999 submission to the ETA Regional Administrator, the Commonwealth asserted that the appended documentation, which had been prepared by the Lynn SDA to satisfy the Commonwealth's requirements for the release of FY 1996 JTPA Title II funds, shows \$1,827,340 in valid expenses under the FY 1996 Title II grants which totaled \$2,080,188. GX 3 at 3, 29-723. Thus, the Commonwealth estimated that the proper amount of disallowed Title II costs for FY 1996 is \$252,848. *Id.* The Commonwealth also submitted performance data for FY 1995 and FY 1996 Title

II grants in an attempt to show that Title II participants were served by the Lynn SDA. GX 3 at 3, 725-54.

The Grant Officer stated in his Revised Final Determination that he found inconsistencies in the documentation and the summary analysis submitted by the Commonwealth, and he stated that no documentation was provided to demonstrate that the Lynn SDA actually used the JTPA Title II funds for the intended purposes. GX 2 at 10. The Grant Officer concluded that the Title II expenses which the Commonwealth sought to validate should have been verified by an “A-133 Audit or a special procedures audit.” *Id.* Consequently, the entire \$2,080,188 remained disallowed.

Regarding the Grant Officer’s Revised Final Determination on the Commonwealth’s request to reduce the amount of disallowed JTPA Title II costs for FY 1996, Mr. Lonergan testified that he reviewed the documentation submitted and drafted a response which became part of the Revised Final Determination. TR 41, 85. He testified that the documentation consists of a list of payment vouchers, copies of documents submitted by NET to the Commonwealth requesting funds, and documents from the Commonwealth approving the issuance of payment vouchers. TR 31, 36, 43-46. As examples of the gaps and inconsistencies he found in the Commonwealth’s evidence, Mr. Lonergan stated that he could not find documentation relating to Voucher No. 61730229/06-28 for \$22,107 and “Advance FY 95” in the amount of \$505,000. TR 46. Although he admitted on cross-examination that the Commonwealth had submitted documentation concerning the \$22,107 amount in Voucher No. 61730229/06-28, TR 86, 109, Mr. Lonergan testified that the documentation did not show that the Lynn SDA actually paid the salaries/vendors as intended. TR 48, 120. He also testified that documentation demonstrating that the Lynn SDA used the funds released by the Commonwealth to pay the salaries/vendors for which they were intended was consistently absent from the package of weekly invoice documentation and showed that the documentation did not comply with generally accepted accounting principles (GAAP). TR 48-51, 120. As additional examples, he cited the Commonwealth’s documentation relating to amounts for \$70,000 (GX 3 at 83-85, 90) and \$41,556 (GX 3 at 154-56), noting that it did not include copies of invoices and checks that would show that the expenditures complied with GAAP. TR 48-51. Mr. Lonergan further noted that in disallowance decisions issued to the City of Lynn, the Commonwealth itself had not accepted this documentation as sufficient to allow the claimed JTPA costs. TR 51.

Mr. Lonergan testified that he rejected the Commonwealth’s recap sheet on the basis that the total amount in the payment column (\$1,754,140) did not equal the amount the Commonwealth claimed in its June 28, 1999 letter as valid Title II expenses. TR 46; GX 2 at 10. However, Mr. Lonergan acknowledged that he had compared expenses with payments in concluding that there was a discrepancy in the Commonwealth’s figures, and he admitted that expenses could exceed payments. TR 88. In this regard, the Commonwealth points out in its post-hearing brief that the FY 1996 Title II payment total of \$2,080,188 cited in its June 28, 1999 letter matches the FY 1996 payment totals shown on its first recap sheet for the three Title II programs – Title IIA (\$958,083), Title IIB (\$996,510) and Title IIC (\$125,595). Commonwealth’s Memorandum of Law at 9-10.

David Manning, the Commonwealth's JTPA Program Manager, testified that the claimed total of \$1,827,340 in allowable FY 1996 Title II expenses is set forth on the second recap sheet submitted by the Commonwealth to the Grant Officer. TR 413. Thus, the Commonwealth's figure of \$252,848 in disallowed FY 1996 Title II expenses is arrived at by subtracting the \$1,827,340.00 in claimed allowable expenses from the total of \$2,080,188 in FY 1996 Title II payments as reflected on the recap sheets.

In its June 28, 1999 correspondence to the ETA Regional Administrator, the Commonwealth also submitted performance data for the FY 1995 and 1996 Title II program. GX 3 at 725-54. The Commonwealth contends that this data "clearly show that Title II participants were served." GX 3 at 3. Alice Sweeney, an DET witness called by the Commonwealth, testified that the performance data was generated by the SDAs and that the figures are verifiable by monitoring. She further testified that DOL never questioned the performance data and that she had spoken to DOL officials about recognizing the Lynn SDA as a high performer in Fiscal Year 1995, although no award was ever made, apparently because of the subsequently discovered record keeping deficiencies. TR 458-60. On cross examination, Ms. Sweeney conceded that it is possible to have a situation where performance statistics show that an SDA is doing a great job although it does not have documentation to support its JTPA costs. TR 481.

3. JTPA Title III Costs

During the funding periods in question, oversight responsibility for the Title III program was conducted by the Corporation for Business, Work and Learning (CBWL) or its predecessor, the Industrial Services Program (ISP). As discussed above, the Commonwealth became aware during FY 1995 that the Lynn SDA and NET was not adhering to JTPA regulations or the policies set forth by its Title III oversight entities, CBWL and ISP. As a result of these deficiencies, CBWL/ISP assumed responsibility during FY 1995 for direct operation of some JTPA Title III programs previously administered by the Lynn SDA, and it began to exercise extensive oversight of other Title III programs before releasing any JTPA funds to NET. GX 3 at 4; TR 320-23. Elizabeth Durkin, the Director of Monitoring for CBWL/ISP, testified that these restrictions consisted of only giving NET formula funds and, beginning in FY 1996, funding NET on a quarter-by-quarter basis. TR 324. Prior to releasing any funds to NET, CBWL/ISP staff reviewed supporting documentation such as invoices, checks, bank statements, payroll records and attendance records submitted by NET to support funds requests. TR 328-30, 350. CBWL/ISP staff also contacted vendors to ensure that the vendors had received and cashed those checks issued by NET. TR 330. Ms. Manning testified that the CBWL/ISP's monitoring and contacts produced positive results, and she was satisfied that the funds disbursed to NET were used for valid JTPA purposes. TR 329-30. Ms. Manning further testified that the supporting documentation obtained from NET was audited as part of an independent audit of

CBWL/ISP, and no problems were identified with respect to the JTPA checks issued to NET. TR 334, 350-51.¹²

In its June 28, 1999 correspondence to the ETA Regional Administrator, the Commonwealth submitted the monthly Fiscal Status Reports (FSRs) which it had required of NET and copies of cash requests from NET and checks disbursed to NET by CBWL/ISP during FY 1995 and FY 1996. GX 2 at 145-365; GX 3 at 4. The Commonwealth acknowledged \$325,113.18 in disallowed costs as a result of its analysis of NET's reconciliation of expenditures and cash for FY 1995 and the FSRs submitted by NET to CBWL/ISP in FY 1996. GX 3 at 4. The Commonwealth also stated when NET closed operations during FY 1995, CBWL/ISP established a procedure for JTPA vendors to request payment directly from CBWL/ISP. Regarding these vendor claims, the Commonwealth stated that it had previously submitted documentation showing direct payments totaling \$8,682 from CBWL/ISP to vendors for services provided to JTPA recipients, and it submitted further documentation showing an additional \$46,616.31 in direct payments from CBWL/ISP to vendors, for a total of \$55,298.31 in direct payments. *Id.* at 5. Finally, the Commonwealth submitted documentation showing \$89,248.69 for payments made by the CBWL/ISP for expenses incurred in connection with the closure of NET during FY 1996, and it reiterated its conclusion that there are a total of \$325,113.18 in properly disallowed JTPA Title III costs for FY 1995 and no disallowed costs for FY 1996 as the CBWL/ISP had only released cash to NET or made direct payments to vendors where there was substantiating documentation. *Id.*

Mr. Lonergan testified that he reviewed the FSRs, cash requests and checks disbursed but was not able to identify a particular FSR that related to a particular cash request or check disbursed because there was "no road map." TR 56. Mr. Lonergan further testified that the documentation submitted by the Commonwealth did not comply with GAAP because there was no documentation to establish that NET actually paid salaries or vendors with the funds, and he concluded that there was no way to determine what costs were allowable because there was no verification of costs and no audit had been performed. TR 57-59. Testifying for the Commonwealth, Ms. Durkin admitted that the documentation submitted to the Grant Officer consisted of "just the funds request and checks issued" and did not include "backup" records such as vendor invoices and checks. TR 351. The Grant Officer's Revised Final Determination confirmed the continued disallowance of the \$325,113.18 in JTPA Title III costs for FY 1995, and it disallowed the \$55,298.31 in direct payments and \$89,248.69 in NET closing costs because the claimed costs had not been verified by an A-133 or special procedures audit. GX 2 at 10-11.

¹² No audit report was submitted to the Grant Officer or offered in evidence.

4. Other Items Resubmitted by the Commonwealth for Consideration

The record shows that the Commonwealth, in February 1999, had previously submitted documentation to the Grant Officer in an effort to reverse the disallowance of JTPA Title III expenditures. The documentation primarily consists of checks issued by NET to training vendors, and it is summarized on two "Payables" sheets which respectively list a total of \$76,031.85 in Title III payments to vendors for FY 1995 and a total of \$182,466.93 in Title III payments to vendors in FY 1995. GX 4 at 1, 87. The Commonwealth also submitted documentation showing direct payments totaling \$8,682 from CBWL/ISP to training vendors. GX 2 at 11; GX 4 at 227-70. And, in its June 28, 1999 correspondence to the ETA Regional Administrator, the Commonwealth stated that its submission included documentation showing an additional \$46,616.31 in direct CBWL/ISP payments to training vendors. GX 2 at 5.

Ms. Durkin testified that the checks issued by NET to the training vendors were made from an advance of \$258,783.13 in JTPA funds from CBWL/ISP. She further testified that CBWL/ISP staff went on-site and verified that the checks were actually issued to the vendors. TR 333. Mr. Lonergan testified that he reviewed this additional Title III documentation submitted by the Commonwealth but was able to identify check copies and supporting information for only \$60,750 in costs from the FY 1996 payables list and \$89,173 from the FY 1996 list. TR 62-64. Mr. Lonergan stated that the balance of costs from both lists did not have sufficient supporting documentation to consider allowing costs. TR 63-64. Although he stated that the \$8,682.00 in checks written by CBWL/ISP to the Boston Electrology Training Center (GX 4 at 227-51) and to Clark University (GX 4 at 252-70) appeared to be legitimate JTPA payments to vendors for services, TR 61-62, Mr. Lonergan maintained that none of the supporting documentation submitted by the Commonwealth was adequate for a determination that expenditures were in compliance with the JTPA regulations because the records had not been subjected to an audit. TR 64-65. With respect to the \$46,616.31 in additional Title III direct payments by CBWL/ISP to vendors referred to in the Commonwealth's June 28, 1999 submission, Mr. Lonergan testified that he found only one check in the amount of \$24,000 to the Computer Career Center accompanied by supporting documentation. TR 65-67; GX 2 at 429-43. Thus, he stated that he did not find documentation for the remaining \$22,616.31 in additional direct CBWL/ISP Title III payments claimed by the Commonwealth. TR 65-68.

The Grant Officer concluded in his Revised Final Determination that none of the claimed payments and expenses could be considered allowable because the origin of the funds used was unclear and the costs were never subjected to an audit. GX 2 at 11. However, the Grant Officer did state that \$8,682 in expenses documented by the checks issued by CBWL/ISP to training vendors could have been considered allowable if they had been verified by an audit. *Id.* The Grant Officer similarly concluded that the additional costs in the amount of \$24,000 could have been considered allowable if the costs had been verified by an audit, but the balance of \$22,616.31 in CBWL/ISP

direct payments could not be allowable in the absence of “properly audited copies of checks and supporting documentation.” *Id.*

5. Expenses Incurred in Closing NET

As discussed above, the JTPA costs claimed as allowable by the Commonwealth include expenditures made by CBWL/ISP in connection with the closing of NET and the Lynn SDA in FY 1996. As part of the records submitted to the ETA Regional Office, the Commonwealth submitted documentation showing direct vendor payments of \$55,298 and expenses of \$89,248 incurred by the Commonwealth in the closing of NET. GX 3 at 6. Referring to the documentation found at pages 367-69 of GX 2, Ms. Durkin testified that CBWL/ISP made a direct payment to a utility company, the Massachusetts Electric Company, in order for the utility company to turn the electricity back on so that staff could gain access the NET facility, remove equipment and secure records. TR 334-35. According to Ms. Durkin, the payment to Massachusetts Electric is a fair representation of the other payments and, like other CBWL/ISP checks, was subject to an audit. TR 351.¹³

Mr. Lonergan testified that he reviewed this documentation and determined that there was no summary sheet indicating what expenses were for closing NET and what expenses related to CBWL/ISP’s direct operation of the JTPA program. TR 70-71. He further testified that the documentation did not indicate the source of the funds used for these expenses, and he rejected the proposed allocation of costs between those for direct vendor payments and those for closing NET. TR 71. Mr. Lonergan explained that clarification of the source of funding is important in order to properly allocate costs between JTPA funds designated for NET and JTPA funds that could be used by the State. TR 71-72. He also noted that the costs claimed as allowable by the Commonwealth had not been subjected to an audit. *Id.* Finally, Mr. Lonergan testified that he had reviewed time sheets submitted by the Commonwealth for work performed by CBWL/JSP personnel in connection with the problems with the JTPA Program at the Lynn SDA. GX 3 at 755-82. In this regard, he stated that it was difficult to determine whether the time indicated was spent in closing down NET and that the Commonwealth did not calculate any specific amount for the time reflected on the time sheets. TR 72-73. The Grant Officer adopted Mr. Lonergan’s recommendations and concluded that the payments and expenses claimed by the Commonwealth in connection with the closure of NET could not be considered allowable unless the origin of the funds used was clarified and the costs subjected to an audit. GX 2 at 11.

¹³ As previously noted, no audit report was submitted to the Grant Officer or offered in evidence.

6. Summary of Disallowed Costs

The Commonwealth contends that it has submitted documentation which shows that the actual amount of properly disallowed JTPA costs is \$1,829,646 or \$1,504,533 for Title II and \$325,113 for Title III. Commonwealth's Memorandum of Law at 15. The Grant Officer rejected the documentation and arguments submitted by the Commonwealth on remand, and he concluded in his Revised Final Determination that JTPA costs in the amount of \$9,107,986.00 remained disallowed. GX 2 at 12. The Grant Officer did acknowledge that the Commonwealth had submitted adequate documentation to support allowance of \$182,605 in JTPA expenditures if they had been verified by an A-133 or special procedures audit. However, he concluded that all costs must remain disallowed because without an audit, "there is no way for ETA to know if the organizations that received the funds provided services to eligible JTPA participants or, if the costs were for administration, whether the costs were within the cost ceiling for administrative expenditures." *Id.* At the hearing, Mr. Salgado confirmed, "There's no way I could reasonably allow any cost without the audit." TR 139.

C. Discussion and Conclusions

1. Disallowed Costs

Section 164(d) of the JTPA "imposes on a recipient the financial liability to repay any amount not properly expended." *Arizona Department of Economic Security v. U.S. Department of Labor*, USDOL/OALJ Reporter, Case No. 94-JTP-18 at 3 (ARB June 7, 1996), *aff'd* 125 F.3d 857 (9th Cir. 1997) (table), 1997 WL 632593 (unpublished opinion). The JTPA regulations provide that the Department shall bear the burden of production to prepare and file and administrative file in support of the Grant Officer's decision to disallow expenditures and that the party seeking to overturn the Grant Officer's decision shall thereafter bear the burden of persuasion. 20 C.F.R. §636.10(g) (1997). In *Texas Department of Commerce v. U.S. Department of Labor*, 137 F. 3d. 329 (1998) (*Texas Commerce*), the United States Court of Appeals for the Fifth Circuit addressed the nature and extent of these respective burdens and held:

Texas Commerce [the JTPA grant recipient] was required to maintain records adequate to show that JTPA funds were spent lawfully. These records enable the DOL to audit these JTPA programs to determine which expenditures should be allowed. Texas Commerce does not bear the initial burden of justifying its expenditures before the ALJ, however. That burden rests upon the DOL which must produce evidence sufficient to establish a *prima facie* case. This requires evidence sufficient for a reasonable person to conclude that JTPA funds were spent unlawfully. If the records of Texas Commerce were inadequate to show that JTPA funds were spent lawfully, the DOL could meet its burden by establishing the inadequacy of the records.

137 F. 3d. at 332 (footnotes omitted). *See also Louisiana v. U.S. Dept. of Labor*, 108 F.3d 614, 617-18 (5th Cir.1997), *cert. denied*, 522 U.S. 823 (1997); *Montgomery County v. Dept. of Labor*, 757 F.2d 1510, 1513 (4th Cir.1985); *State of Maine v. U.S. Dept. of Labor*, 669 F.2d 827, 830 (1st Cir.1982) (discussing the burdens of production and persuasion under the Comprehensive Education and Training Act, CETA, which the JTPA superceded).

In the Revised Final Determination, the Grant Officer did not accept the documentation submitted by the Commonwealth on remand to support the disallowed JTPA costs, asserting that the documents are inadequate to allow the Grant Officer to determine which expenditures should be allowed because they had not been subjected to an A-133 audit. GX 2 at 9-12. Section 164(a) of the JTPA states that “[a]t least once every two years, the State shall prepare or have prepared an independent financial and compliance audit of each recipient of funds under titles II and III of this Act.” 29 U.S.C. §1574(a)(2) (1982). The JTPA regulations at 20 C.F.R. §627.480(a) require governmental recipients of JTPA funds to comply with the Single Audit Act of 1984, 31 U.S.C. §§7501-7507, and the regulations at 29 C.F.R. Part 96. The Part 96 regulations in effect during the period of the JTPA grants in question in this proceeding required state and local governmental recipients of Federal assistance in excess of \$100,000 to have an audit performed annually. 29 C.F.R. §96.101 (1998). Responsibility for ensuring compliance with the audit requirement is placed on the recipient of Federal assistance. 29 C.F.R. §96.54 (1998). Similarly, the Commonwealth’s Policy Directive 94-07 (October 6, 1994) states that “[c]onsistent with federal regulations, DET policy has required each SDA obtain an annual financial and compliance audit of JTPA funds.” GX 2 at 655. Thus, it is clear that the JTPA and implementing regulations required an annual independent audit of the Lynn SDA. Since there is no dispute that the required audit of the Lynn SDA was not performed for any of the fiscal years at issue, the threshold question presented is whether the showing that no audit was performed is sufficient to meet the Grant Officer’s burden of producing evidence sufficient for a reasonable person to conclude that JTPA funds were spent unlawfully.¹⁴

¹⁴ It is noted that the parties have devoted considerable time and energy in this proceeding to the question of whether OMB Circular A-128 or A-133 governed the annual audits required during the fiscal years in controversy. While I find it unnecessary to resolve this controversy in light of the fact that no audit, either A-128 or A-133, was conducted, it seems that both parties are partially right on this somewhat arcane point. The Single Audit Act was amended in 1996 for fiscal years beginning after June 30, 1996. Pub.L.104-156, §2 (July 5, 1996), 110 Stat. 1396. Thereafter, the Part 96 Regulations were amended to change the reference from OMB Circular A-128 to OMB Circular A-133 for the annual audits required of all recipients and subrecipients of DOL funds for fiscal years beginning after June 30, 1995. 29 C.F.R. §§96.11, 96.12; 64 FR 14539 (March 25, 1999). Thus, it appears that the requisite audit for FY 1995 should have been conducted pursuant to OMB Circular A-128, while the audits for subsequent fiscal years would be subject to OMB Circular A-133.

The Department cites no authority which specifically holds that a JTPA grant recipient's failure to comply with the audit requirements perforce establishes that the JTPA funds were expended unlawfully. However, the courts have consistently held that the record keeping requirements of the JTPA and its predecessor act, CETA, are critical to the oversight and evaluation provisions and that a recipient's failure to comply with record keeping requirements amounts to an unlawful spending of funds. *Louisiana v. U.S. Dept. of Labor*, 108 F.3d 614, 618 (5th Cir.1997), *cert. denied*, 522 U.S. 823 (1997); *Montgomery County v. Dept. of Labor*, 757 F.2d 1510, 1513 (4th Cir.1985); *City of Oakland v. Donovan*, 703 F.2d 1104, 1107 (9th Cir. 1983), *modified*, 707 F.2d 1013. The *Louisiana* case is particularly instructive. There, the state disbursed JTPA funds to a SDA which failed to maintain records concerning its expenditure of those funds as required by section 165 of the JTPA. Under those circumstances, the Court upheld Department's decision to disallow the challenged expenses and require repayment by the state:

Substantial evidence supports the conclusion that Louisiana utterly failed to maintain accurate and reliable financial records, in violation of 29 U.S.C. §1575(a)(1), and the Secretary correctly held that such nonfeasance constitutes a violation of the JTPA. Therefore the Secretary properly denied the challenged expenses and ordered the state to repay the disallowed expenses.

108 F.3d at 618. As outlined above, the JTPA's oversight and evaluation scheme contains specific audit requirements at section 164 in addition to the record keeping requirements at section 165. In my view, the JTPA's audit requirements are as integral to the oversight and evaluation process as the record keeping requirements, and the Commonwealth's failure to fulfill its audit responsibilities under section 164 is no less a nonfeasance than was Louisiana's failure to comply with the record keeping requirements under section 165. Consequently, I conclude that the Grant Officer, by showing that the Commonwealth failed to comply with the audit requirements, has met its burden of producing evidence of a *prima facie* violation of the JTPA; that is, evidence sufficient for a reasonable person to conclude that the disallowed funds were misspent within the meaning of section 164(d).

Next to be considered is whether the Commonwealth has carried its burden of persuasion to show that, notwithstanding the failure to conduct the required audits, any of the disallowed costs were properly expended for lawful JTPA purposes. As an initial matter, I find that the instant case is distinguishable from *Montgomery County v. Dept. of Labor*, 757 F.2d 1510 (4th Cir.1985) where the Court affirmed disallowance of the full amount of challenged JTPA costs. In that case, the Grant Officer allowed all expenditures for which the county could provide documentation but disallowed the remainder, regarding which the evidence established that the supporting records were "unauditable" (sic). 757 F.2d at 1512. Although the county offered abundant testimony that training services were provided in a satisfactory manner, the Court affirmed disallowance of the costs for which there was inadequate documentation. *Id.* at 1512-1513. Here, the Commonwealth has reconstructed records and introduced substantial, uncontradicted evidence that certain of the disallowed costs were expended for appropriate JTPA purposes. Accordingly, I find that to the extent that challenged costs are

supported by the documentation submitted by the Commonwealth, such costs should be allowed. *See Commissioner, Employment Security of the State of Washington v. U.S. Dep't of Labor*, USDOL/OALJ Reporter (HTML), OALJ Nos. 90-JTP-29, 91-JTP-11 and 92-JTP-34 (Sec'y September 13, 1995) (ALJ reversed Grant Officer's disallowance of costs for which complainant produced evidence of documented participant benefits).

As discussed above, the Commonwealth submitted a Reconstructed Trial Balance for FY 1995 Title II expenses which is based on a reconstruction of financial records performed by a certified public accountant. The reconstructed records show that \$4,861,178 in JTPA Title II costs for FY 1995 were properly expended and that \$1,049,280 in costs were properly disallowed. Aside from asserting that the reconstruction must be rejected *in toto* because of the absence of an audit, the Department did not offer any contrary evidence. Accordingly, I find that \$4,861,178 in JTPA Title II costs for FY 1995 should have been allowed.

In contrast to the reconstruction of the Title II documentation for FY 1995, Mr. Lonergan testified without contradiction the weekly invoice records for FY 1996 submitted by the Commonwealth consistently lacked supporting documentation such as such as copies of individual invoices and checks which show that the expenditures complied with GAAP and were actually made for appropriate JTPA purposes. TR 48-51. While the Commonwealth's witnesses testified that DET staff reviewed NET's records during on-site visits, verified vendor checks against bank statements and contacted vendors to verify that they had actually received the payment, TR 451-53, none of these records were submitted to the Grant Officer. On this record, I am constrained to find that the Commonwealth's Title II documentation for FY 1996, like the documentation in *Montgomery County*, is "unauditable" and, therefore, insufficient to support allowance any of the challenged \$2,080,188 in JTPA Title II costs for FY 1996.

For the same reason, I also find that the Grant Officer properly disallowed the majority of the JTPA Title III costs claimed by the Commonwealth. As the Commonwealth's own witness, Ms. Durkin, conceded, supporting documentation such as vendor invoices and checks were not submitted for these costs, "just the funds request and checks issued." TR 351. However, the Revised Final Determination and Mr. Lonergan's testimony establish that the Commonwealth did submit adequate documentation to support allowance of \$182,605 in JTPA Title III expenditures for FY 1995 and 1996, including \$8,682 in direct payments by CBWL/ISP to vendors and \$24,000 in NET closing costs incurred by CBWL/ISP, if only they had been subjected to an audit. GX 2 at 12. As I have determined that an audit is not a *sine qua non* for allowance of JTPA expenditures supported by adequate financial records, I conclude that \$182,605 in JTPA Title III costs must be allowed.

In sum, I find that a total of \$5,043,783 in JTPA costs for the years in question are supported by adequate documentation and hereby allowed. The remaining costs in the amount of \$4,064,203 are not supported by adequate record and were properly disallowed.

2. The Commonwealth's Eligibility for Waiver

Section 164(e)(3) of the JTPA provides for the waiver of the imposition of sanctions against a state due to a subrecipient's misexpenditure of JTPA funds, if the state can adequately demonstrate that it substantially complied with the requirements set forth in section 164(e)(2). 29 U.S.C. §1574(e)(3); *Commonwealth of Pennsylvania Department of Labor and Industry v. U.S. Department of Labor*, USDOL/OALJ Reporter (HTML), OALJ No. 92-JTP-12 at 3 (Sec'y March 5, 1995); *State of Washington v. U.S. Department of Labor*, USDOL/OALJ Reporter (HTML), OALJ No. 90-JTP-29 at 4 (Sec'y September 13, 1995). Section 164(e)(2) of the JTPA provides:

(2) In determining whether to impose any sanction authorized by this section against a recipient for violations by a subgrantee of such recipient under this Act or the regulations under this Act, the Secretary shall first determine whether such recipient has adequately demonstrated that it has--

(A) established and adhered to an appropriate system for the award and monitoring of contracts with subgrantees which contains acceptable standards for ensuring accountability;

(B) entered into a written contract with such subgrantee which established clear goals and obligations in unambiguous terms;

(C) acted with due diligence to monitor the implementation of the subgrantee contract, including the carrying out of the appropriate monitoring activities (including audits) at reasonable intervals; and

(D) taken prompt and appropriate corrective action upon becoming aware of any evidence of a violation of this Act or the regulations under this Act by such subgrantee.

29 U.S.C. §1574(e)(2). In an effort to demonstrate that it satisfied the subparagraph (A) criterion for a waiver, *i.e.*, that it established and adhered to an appropriate system for the award and monitoring of contracts with subgrantees, the Commonwealth submitted copies of several Policy Directives and Policy Letters that it issued to its grantees. GX 2 at 537-912. The Grant Officer denied the Commonwealth's request for a waiver, in part based on a determination that the Commonwealth failed to adhere effectively to these policies. GX 2 at 13. In this regard, the Grant Officer testified that he found that the Commonwealth did not meet the requirements of subparagraph (A) because, in contravention of its own policies, it did not adequately monitor its subgrantee. TR 156, 194-96.

One of the Commonwealth's JTPA grant policies, Policy Directive 93-12, provides for four possible outcomes from review of a subgrantee's administrative systems – certified, certified with conditions, out of compliance and decertified. GX 2 at 542-43. Under this policy, a “certified with

conditions” rating requires corrective action within specified time frames or the subgrantee’s status will be downgraded to “out of compliance” and, eventually, “decertified”. *Id.* at 542. As the Department notes, the Commonwealth conditionally certified NET’s fiscal system as early as October 1993, but it did not decertify the fiscal system until April 10, 1996. GX 1 at 190-91. Mr. Manning of DET testified that a subgrantee’s status will be changed to “out of compliance” under Policy Directive 93-12 if the requisite standards are not reached within a specified time frame. TR 418. Mr. Manning also testified that the Commonwealth requires a subgrantee to bring its fiscal system into compliance by the following monitoring visit, which is conducted annually. TR 424. Accordingly, I find that once NET’s fiscal system was given a “certified with conditions” designation in the Fall of 1993, Policy Directive 93-12 required that an “out of compliance” designation be imposed as of the next annual monitoring visit as it is undisputed that the Lynn SDA did not take the necessary corrective actions to bring its fiscal systems back into compliance. This, however, was not done. Instead, CBWL/ISP again conditionally approved NET’s fiscal system on September 12, 1994 despite its findings that (1) NET was eighteen months behind in reconciling bank statements, (2) that NET had no way of determining its actual assets, (3) that NET did not have an acceptable methodology for allocating costs, (3) that reports are not easily traced to the general ledger and (4) that similar findings were contained in the Fiscal Year 1992 audit. GX 2 at 1147-53. On February 21, 1995, the CBWL/ISP stated that “there has been inadequate measurable progress in NET’s Fiscal systems since the last series of technical assistance sessions provided by ISP staff.” GX 2 at 1161. On March 3, 1995, the Commonwealth informed NET that it had “serious concerns about the current condition of Northshore Employment and Training’s financial records and internal controls.” GX 2 at 1235. This letter also states that DET and CBWL/ISP staff had identified numerous problems with NET’s fiscal system based on monitoring during Fiscal Year 1995 as well as prior periods. *Id.* And, in May 1995, ISP took over direct responsibility for certain Title III programs. GX 2 at 1172. Despite these findings, Mr. Manning conceded that the conditional certification of NET’s fiscal system was not changed until April 1996. TR 427. Although Mr. Manning testified that downgrading NET’s status to “out of compliance” earlier likely would not have protected the integrity of the JTPA funds; TR at 405-06; the Grant Officer testified that had the Commonwealth properly adhered to its own fiscal systems monitoring and certification policy, much of the challenged costs for Fiscal Years 1995 and 1996 would not have occurred. TR 158.

On these facts, I conclude that the Commonwealth has not demonstrated that it adhered to an appropriate system for the award and monitoring of contracts with its subgrantees as required by section 164(e)(2)(A). Having failed to comply with its own monitoring policies, the Commonwealth can not avail itself of the JTPA’s waiver of repayment provisions.

III. Order

The Grant Officer’s determination to disallow JTPA costs is **AFFIRMED** in part and **REVERSED** in part. The Grant Officer’s determination to deny the Commonwealth’s request for a waiver of repayment of disallowed costs is **AFFIRMED**. Accordingly, **IT IS ORDERED** that the

Commonwealth of Massachusetts shall repay from non-federal funds the sum of \$4,064,203 to the United States Department of Labor. *Milwaukee County, Wisconsin v. Donovan*, 771 F.2d 983, 993 (7th Cir. 1985).

A

Daniel F. Sutton

Administrative Law Judge

Boston, Massachusetts

DFS:dmd

NOTICE OF APPEAL RIGHTS. Pursuant to 29 USC 1576(b), any party dissatisfied with this decision and order Dismissal may appeal it to the Administrative Review Board within 20 days after receipt of the Order, by filing exceptions specifically identifying the procedure, fact, law, or policy to which exception is taken. Thereafter the decision of the administrative law judge shall become the final decision of the Secretary unless the Secretary, within 30 days of such filing, has notified the parties that the case has been accepted for review. The petition for review may be filed with the Administrative Review Board, United States Department of Labor, Room S-4309, Frances Perkins Building, 200 Constitution Ave., N.W., Washington, D.C. 20210. A copy of any such petition must also be provided to the Chief Administrative Law Judge, Office of Administrative Law Judges, 800 K Street, N.W., Washington, D.C., 20001-8002.